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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1946

LILLIAN JEFFRIES,

Petitioner,

versus

COMMISSIONER OF INTERNAL
REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

TO THE HONORABLE THE CHIEF JUSTICE AND
ASSOCIATE JUSTICES OF THE SUPREME COURT OF
THE UNITED STATES:

This is a petition for a writ of certiorari to review
the decision of the United States Circuit Court of Appeals
for the Fifth Circuit.

JURISDICTION

Jurisdiction of this Court is invoked under Section
240 (a) of the Judicial Code as amended by the Act of
February 13, 1925, c. 229, Sec. 1, (43 Stat. 938). (United
States Code, Annotated, Title 28, Sec. 347). The decision

sought to be reviewed was rendered on November 22, 1946, and application for rehearing, seasonably made and entertained by the Court, was denied on December 24, 1946.

QUESTIONS PRESENTED

This case came to the Circuit Court of Appeals upon a petition for review of a decision of the Tax Court of the United States, which determined a deficiency in income tax of Lillian Jeffries in the sum of \$32,827.36 for the year 1940 (R. 30).

The respondent, Commissioner of Internal Revenue, on May 2, 1944, served upon the petitioner, Lillian Jeffries, a notice of deficiency, (R. 10) who in turn duly filed with the Tax Court of the United States her petition for redetermination of the deficiency (R. 2). Answer was filed by the Commissioner of Internal Revenue, (R. 15) and in due course the cause came on for hearing before Honorable Arthur J. Mellott, one of the Judges of said Court, then and there presiding at Miami, Florida. Thereafter, on December 28, 1945, the Tax Court of the United States promulgated its findings of fact and opinion, and on December 29, 1945, its decision determining the deficiency was entered (R. 16, 29). Thereafter, on March 13, 1946, the petitioner filed her petition for review by the Circuit Court of Appeals (R. 30). The Circuit Court of Appeals on November 22, 1946, affirmed the decision of the Tax Court of the United States, (R. 40) and on December 24, 1946 denied rehearing (R. 58).

The facts upon which the deficiency is alleged to have arisen are, briefly, as follows:

Girard Realty Company was originally organized by J. B. Jeffries, William L. Austin and a third person for the purpose of acquiring and holding title to a large tract of undeveloped lands in the Everglades section of Florida (R. 18).

Many years ago, and prior to 1932, a portion of the lands was disposed of and the corporation reorganized and continued for the purpose only of holding title to said lands. Upon the reorganization J. B. Jeffries and William L. Austin each owned fifty per cent of the capital stock of the corporation. In 1932 Austin died, and in 1936 Jeffries died. The Executors of the Austin Estate succeeded to the stock owned previously by Austin, and Mrs. Jeffries succeeded to the stock owned previously by her husband. (R. 18).

The corporation did no business and had no income, but on the contrary it was necessary from year to year for Austin and Jeffries to personally contribute the funds necessary to pay State, County and Drainage District taxes. After the death of Austin and Jeffries these taxes were not paid as they became due, and finally in 1939 there was a large accumulation of unpaid State, County and Drainage District taxes. The property was about to be lost for taxes. Mrs. Jeffries called upon the Austin Estate to contribute one-half of the money necessary to redeem the lands from tax sale. The Austins refused, and Mrs. Jeffries advanced the money for the purpose of paying the taxes, taking mortgages on the property of the company to secure the sums so advanced. A dispute arose between Mrs. Jeffries and the Austins and she began foreclosure of her mortgage. Whereupon the heirs and

executors of the Austin Estate intervened in the foreclosure and had themselves made parties defendant and the case thereupon proceeded as a suit between Mrs. Jeffries and the executors and heirs of the Austin Estate. (R. 18, 19).

The Austins in their pleadings charged Mrs. Jeffries with fraud, and considerable feeling arose between the parties to the litigation. Finally a settlement of all of their differences was agreed upon between Mrs. Jeffries and the Austins. It was agreed that a portion of the property would be sold for the purpose of securing the funds with which to reimburse Mrs. Jeffries for her advances and for the payment of attorneys and auditors, and that all of the remaining assets of the corporation would be equally divided between the two stockholders—Mrs. Jeffries and the Austins. An agreement embodying the terms of the settlement was prepared, signed by Mrs. Jeffries and forwarded to Philadelphia to be executed by the Austins. A sale was consummated of a portion of the lands which it was agreed would be sold, and the parties met for the purpose of putting the settlement into effect. At that meeting the Austins stated that their Estate was still in the process of administration and they had no one who could take title to the half of the property being allocated to them, and requested Mrs. Jeffries to accept deed to her half of the property, surrender her stock in the corporation, and allow the Austins to retain title to their half of the property being received in the settlement, in the name of the corporation. Mrs. Jeffries was suspicious of consummating the settlement and refused to permit it to be done in that way. However, upon assurance of her own attorneys and an income tax expert that this method

of handling it in no way changed her legal or income tax status, she consented for the matter to be handled in that way. The net result was that the assets of Girard Realty Company were equally divided between Mrs. Jeffries and the Austins, Mrs. Jeffries taking title to her half in her own name and the Austins retaining the title to their half in the name of Girard Realty Company. The lawsuit was settled and dismissed and the Austins executed releases exonerating Mrs. Jeffries of the charges which had been made against her in the litigation (R. 19, 20, 21).

Mrs. Jeffries thereupon caused the lands received by her in the settlement to be appraised by an appraiser for the Federal Land Bank. She believed that the appraisal so made was inadequate and she voluntarily increased the appraised value of the property to a much higher figure (R. 24).

Mrs. Jeffries thereupon reported as income for 1940 the difference between the amount which she had paid at a "wash sale" of her stock and the value of the property as fixed by her, which was an amount greatly in excess of the appraised value of the property. She reported this as a long term gain and promptly paid her taxes on it in the sum of \$18,169.47 (R. 24, 25, 11). Thereafter the Commissioner of Internal Revenue served notice upon Mrs. Jeffries of an alleged deficiency in her tax for 1940, based upon the contention that the gain realized by her in the acceptance of said property was a short term gain rather than a long term gain, because, as he contended, the property had been received by her in partial liquidation of the corporation (R. 10, 12, 25). The issues submitted to the Tax Court of the United States were these:

Respondent contended that because Mrs. Jeffries surrendered her stock and accepted a deed to her half of the property, whereas the Austin Estate retained title to their half in the name of the corporation, the transaction constituted a partial liquidation of a corporation and was taxable under the provisions of Section 115(c) of the Revenue Act of 1938 (then in effect, but since repealed) as a short term gain. (R. 12, 25).

The petitioner contended that the transaction was an equal division of the assets of the corporation between herself and the Austin Estate in settlement of a lawsuit and was not a partial liquidation of the corporation; that the division was complete, and that each stockholder received one-half of the assets of the corporation; that the fact that the Austins permitted their half of the property to remain in the name of the corporation did not alter or change the effect (R. 25, 26).

Petitioner contended that Section 115(c) aforesaid was intended by Congress to cover only ordinary dividends distributed under the guise of distributions in partial liquidation and that Congress never intended said Section to apply to unquestionable bona fide redemptions of stock not equivalent in any way to the distribution of a taxable dividend; and that said Section did not apply to the division of assets which was accomplished by the transaction here under consideration (R. 25, 26).

Petitioner contended that the entire transaction must be considered and the net results obtained must determine the character of the transaction, and that the component parts of the transaction could not be considered separate-

ly for the purpose of determining its character, and that substance, rather than form, should control (R. 27).

Petitioner contended that her gain (enhanced value of the property received) was a long term gain and taxable as such, and that since she had paid the full amount of taxes chargeable on that basis, the alleged deficiency should be disallowed (R. 24).

Following the determination of the deficiency by the Tax Court of the United States, the petitioner filed with the Circuit Court of Appeals her petition for review, assigning as errors the following acts and omissions of the Tax Court of the United States:

1—The findings of the Tax Court of the United States that there was a partial liquidation of Girard Realty Company.

2—The refusal of the Tax Court of the United States to consider the intent of the parties and to give effect to that intent in construing the effect of the transaction whereby Petitioner received one-half of the assets of Girard Realty Company.

3—The finding of the Tax Court of the United States overruling and denying the contention of Petitioner that the provisions of Section 115(c) of the Revenue Act of 1938 (since repealed) were intended by Congress to apply only to the distribution of taxable dividends disguised as distributions in liquidation, and did not apply to bona fide redemptions of stock.

4—The findings of the Tax Court of the United States whereby it construed only the fact that Petitioner surrendered her stock in Girard Realty Company and received one-half of its assets, and refused to consider the entire transaction and give effect to the intent of the parties, which was that there should be a complete division of the assets of the corporation between two groups of stockholders.

5—The finding of the Tax Court of the United States that the capital gain realized by Petitioner in receiving one-half of the assets of Girard Realty Company constituted a short term gain.

6—The finding by the Tax Court of the United States that there is a deficiency of \$32,827.36 in the income tax of Petitioner for the year 1940.

7—The making an entry by the Tax Court of the United States of its Decision of December 29, 1945 (R. 33, 34).

The Circuit Court of Appeals affirmed the decision of the Tax Court of the United States. This petition for certiorari follows.

REASONS FOR ALLOWANCE OF WRIT

It is respectfully submitted that certiorari should be granted in this case for the following reasons:

1. The present decision is in conflict with the decisions of other Circuit Courts of Appeal and with other decisions of the same Circuit Court of Appeals.

2. The Circuit Court of Appeals has herein decided a federal question in conflict with applicable decisions of the Supreme Court of the United States.

3. The Circuit Court of Appeals has herein decided an important question of federal law which has not been, but should be, settled by the Supreme Court of the United States.

4. The Circuit Court of Appeals has overlooked and failed to pass upon certain essential assignments of error.

5. The Circuit Court of Appeals has misunderstood, and therefore mis-stated, certain essential contentions of the Petitioner.

SUPPORTING BRIEF

General Justice and Equity

In the Majority Opinion the Circuit Court of Appeals said (R. 42):

"Whether a transaction or result is taxable, and what the tax is, is not a matter to be determined in law upon considerations of general justice or equity."

The Majority Opinion in this case is in direct conflict with the pronouncement of the same Court in the case of **Alamo National Bank of San Antonio vs. Commissioner of Internal Revenue**, 95 Fed. (2d) 622, where the court after holding that taxation is a matter of statutes and equitable considerations cannot override the provisions of the statute, nor always supply their omissions, said, (page 623):

"Nevertheless, honesty, good faith, and consistency are due in tax accounting. The right and wrong of things, and equitable principles have a place in tax matters."

The pronouncement in this case, as above quoted, is also in conflict with the decision of the Supreme Court of the United States in the case of **Stone vs. White**, 301 U.S. 532, 81 L. Ed. 1265, 57 S. C. 851, where that court not only recognized equitable pleas, but based its decision upon equitable considerations, and on page 1271 of 81 L. Ed., the court in reaching its conclusion said:

"Equitable conceptions of justice compel the conclusion that the retention of the tax money would not result in any unjust enrichment of the Government."

Repeal of Act

The Circuit Court of Appeals overlooked and failed to pass upon Petitioner's Assignment of Error No. 3, (R. 34) wherein Petitioner assigned as error:

"The finding of the Tax Court of the United States overruling and denying the contention of Appellant that the provisions of Section 115(c) of the Revenue Act of 1938 (since repealed) were intended by Congress to apply only to the distribution of taxable dividends disguised as distributions in liquidation, and did not apply to bona fide redemptions of stock."

In the Majority Opinion the Court said (R. 42):

"Neither will it avail her to point to the fact that Congress in 1942, recognizing the inequities of Section 115(c), repealed the provision taxing a partial liquidation as a short term gain, without making the repeal retroactive."

The Court appears to have misunderstood the contention of the Petitioner and appears to have believed that Petitioner contended that Section 115(c) should be disregarded because it has since been repealed. This was not the contention of Petitioner, as set forth in the Assign-

ment of Error No. 3 nor does it follow Question No. 1, as set forth in the questions for determination in the Petition for Review (R. 32). The question as presented in the Assignments of Error and the Petition for Review is that it never was the intention of Congress that the provisions of Section 115(c) should apply to bona fide redemption of stock, but that it was the intention of Congress, as reflected by the reports of legislative committees filed at the time of its repeal, that the provisions of this Section should apply only to distributions of taxable dividends disguised as distributions in liquidation.

In 1942 the Congress recognized the injustice of Section 115(c) of the Revenue Code and eliminated it as to taxable years subsequent to 1941. The Senate Finance Committee, in its report on the Revenue Bill of 1942 (Report No. 1631, to accompany H.R. 7378, filed October 2, 1942) on page 116 thereof, in dealing with this Section, said:

"This treatment was occasioned by the facility with which ordinary dividends may be distributed under the guise of distributions in partial liquidation, although Section 115(g) makes explicit provision for the treatment of such distributions as ordinary dividends. Inequality results, however, under the existing law in the case of unquestionable bona fide redemptions of stock not equivalent in any way to the distribution of a taxable dividend. It is believed that the proper application of Section 115(g) will prove adequate to prevent taxable dividends disguised as liquidations from receiving capital-gain treatment. Accordingly, this Section of the Bill eliminates the pro-

vision requiring the gain from a partial liquidation to be treated as a short-term capital gain."

This Petitioner has never contended that the mere repeal of a section of the statutes, regardless of its inequity or unreasonableness, would have a retroactive effect. On the other hand Petitioner contended both in the Tax Court and in the Circuit Court of Appeals that in determining legislative intent the Court could and should consider the solemn declarations of Congressional Committees, including those filed with the repeal of the Section; it was the further contention of Petitioner that the statement set forth in the legislative committee's report is a clear and unmistakable statement that Congress never did intend that this Section should apply to bona fide redemptions of stock.

Intention of Parties

The Circuit Court of Appeals misunderstood and therefore mis-stated the contention of the Petitioner with respect to the effect to be given to the intention of the parties, as set forth in Assignment No. 4 of the Assignments of Error (R. 34).

In the Majority Opinion this Court said (R. 42):

"Because the statutes and regulations read as they do, and the facts are what they are, it will not avail Petitioner to point (1) to the fact that she all along intended to bring about a complete liquidation, and that she regarded the course taken as bringing this about."

Petitioner has never contended that the result of the action taken should be determined solely upon what "she all along intended."

Petitioner's Assignment of Error No. 4 charges as error:

"The findings of the Tax Court of the United States whereby it construed only the fact that Appellant surrendered her stock in Girard Realty Company and received one-half of its assets, and refused to consider the entire transaction and give effect to the intent of the parties, which was that there should be a complete division of the assets of the corporation between two groups of stockholders."

It was the contention of Petitioner that it was the intention of both parties to the transaction that there should be an equal division of the property of the corporation between the two groups of stockholders, and that this was actually accomplished.

It is clear from the Findings of Fact and as reported by the Tax Court that there was a complete distribution of all of the assets of Girard Realty Company; one-half to Mrs. Jeffries and one-half to the Austins. It was not a partial distribution. The distribution was complete and included all of the assets of the Company.

The fact that Mrs. Jeffries took title to her half in her own name, and the fact that the Austins left the title to their half in the name of the Company does not alter

the fact that Mrs. Jeffries got half of the assets and the Austins got the other half. There can be no doubt that what the parties had in mind was to dissolve their relationship and divide their property between them.

Judge Mellott of the Tax Court correctly stated this proposition when he said (R. 29):

"The net effect, therefore, was a complete division of the assets of the corporation between the two groups of stockholders."

In reaching its conclusion the Circuit Court of Appeals undoubtedly also overlooked that provision in the Resolution adopted by the Corporation, wherein the Corporation stated (R. 24):

"It being further resolved that the payment of the monies and the issuance of the deed, as in this Resolution referred to, be and the same are hereby determined to have been made for the purpose of liquidating and dividing the assets of this Company."

Petitioner is fully aware that in determining the intent of parties to a contract the intention of one of the parties alone would not be sufficient. This Petitioner, therefore, never has contended that her intent standing alone would be sufficient to determine the effect of the transaction. What she did contend is that it was the intention of both parties to the transaction that there should be an equal division of the assets of the Corporation between the two stockholders, and that this actually was accom-

plished regardless of the mechanics adopted in its consummation.

Hardship

The Circuit Court of Appeals misunderstood and therefore mis-stated this Petitioner's contention when the Court said, in the Majority Opinion (R. 42):

"It will not avail Petitioner to point * * * to the tax hardships she is being subjected to for a mere mistake in method if the method adopted is found to be a mistaken one."

This Petitioner has never contended that the "hardships she is being subjected to" is a sufficient ground for the reversal of the decision of the Tax Court. The Court's statement leaves the erroneous impression that Petitioner has appealed merely for sympathy and has not based her case upon sound considerations of the law.

Substance vs. Form

In the Majority Opinion the Circuit Court of Appeals held that whether a transaction or result is taxable, and what the tax is (R. 42)

"is a matter of statutes and valid regulations, and what they mean. Neither is it to be determined in fact upon considerations of what was intended to be done. Rather it is to be determined by what was done. * * * Taxation deals not with what was attempted to be done but with what was done."

Under the facts and the contentions of Petitioner in this case, the ruling of the Court above quoted is tantamount to a ruling that the tax liability will be determined solely upon the form and mechanics adopted in the transaction, and that neither the intent of the parties nor the effect of the action, or the results actually accomplished will be considered.

Such a ruling is in direct conflict with the decision of the Circuit Court of Appeals of the Sixth Circuit in the case of **Mather vs. Commissioner**, 149 Fed. (2d) 393; the decision of the Circuit Court of Appeals of the Tenth Circuit in the case of **Prairie Oil & Gas Co. vs. Motter**, 66 Fed. (2d) 308 and the decision of the Supreme Court of the United States in the cases of **Corliss vs. Bowers**, 281 U.S. 376, 74 L. ed. 916, 50 S. C. 336, and **Minnesota Tea Co. v. Helvering**, 302 U.S. 609, 82 L. ed. 474, 58 S. C. 393.

The effect of the four decisions cited, as well as other cases not cited, is that "the substance of the thing done and not the form it took, must govern, and the courts have recognized that where the essential nature of a transaction is the acquisition of property, it will be viewed as a whole, and closely related steps will not be separated either at the instance of the taxpayer or the taxing authority" (149 Fed. (2d) 393, 397).

The effect of that part of the decision of the Circuit Court of Appeals in the present case, above quoted, is to hold that because the form adopted in one step in the transaction conforms to the definition of a partial liquidation, all other steps, as well as the intentions of the parties and the actual results accomplished, are to be ignored.

The above quoted portion of this decision is in conflict with the decision of the Supreme Court of the United States in **Corliss vs. Bowers**, 281 U.S. 376, 74 L. ed. 916, 50 S. C. 336, wherein the Supreme Court on page 917, L. ed. said that

“taxation is not so much concerned with the refinements of title as it is with actual command over the property taxed—the actual benefit for which the tax is paid,” * * *

It makes no difference that such “command” may be exercised through specific retention of legal title or the creation of a new equitable but controlled interest, or the maintenance of effective benefit through the interposition of a subservient agency. As was most aptly stated in **Minnesota Tea Co. vs. Helvering**, 302 U.S. 609, 82 L. ed. 474 at page 477, 58 S. C. 393,

“a given result at the end of a straight path,
* * * is not made a different result because
reached by following a devious path.”

In the present case, the “given result at the end of a straight path” was the acquisition by the Austins of a half of the property; and this result was not changed by the fact that title remained vested in a corporation owned exclusively by them. When Mrs. Jeffries surrendered her stock Girard Realty Company became the mere trustee or repository of the legal title for the lands of the Austins, who were the owners of the beneficial interest. Leaving title in the name of a company exclusively owned by the Austins was just a convenient method of handling it, and

the company thereupon became the repository of the title for them until such time as they decided to sell. The result was the same as if they had caused the title to be vested in some other corporation which they owned.

The following facts were reported by the Tax Court of the United States in its Findings of Fact (R. 21):

"The Girard Realty Co. was not a party to the negotiations between Petitioner and the Austins for the division of the land held by it. The settlement was arrived at by the parties in interest as a division of the property to which the company held title and as a settlement of the foreclosure suit which had been instituted by Petitioner."

We submit that the true rule was stated in the dissenting opinion of Judge Mellott of the Tax Court, where he said (R. 28):

"While I recognize the fact that the mechanics adopted point strongly to a mere partial liquidation of the corporation, actually what occurred was a division of the assets of the corporation in kind, the Austins engineering the whole plan for the purpose of making use of the corporation as the nominal title holder for the portion of the property distributed to them."

We respectfully submit that the Circuit Court of Appeals in the Majority Opinion overlooked this contention of the Petitioner and failed to pass upon the question thus raised.

CONCLUSION

The Circuit Court of Appeals rendered its decision by a divided court. That there was a wide divergence of opinion among the members of that court is clearly shown by the forceful, single sentence dissenting opinion by Judge Waller (R. 43):

"Regardless of the insatiability of Taxation's appetite and the present emptiness of her voracious maw, the courts ought not to try to satisfy one and fill the other by upholding extortions from inexperienced widows when such could be, and should be, avoided by following the salutary rule of looking at the substance of the transaction rather than at its form."

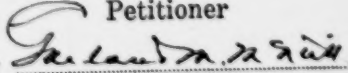
Substance rather than form should control, and the equities of the case should be considered. For the reasons hereinabove set forth, we respectfully ask that this Court grant a writ of certiorari to bring before this Court for review the decision of the Circuit Court of Appeals.

Respectfully submitted,

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